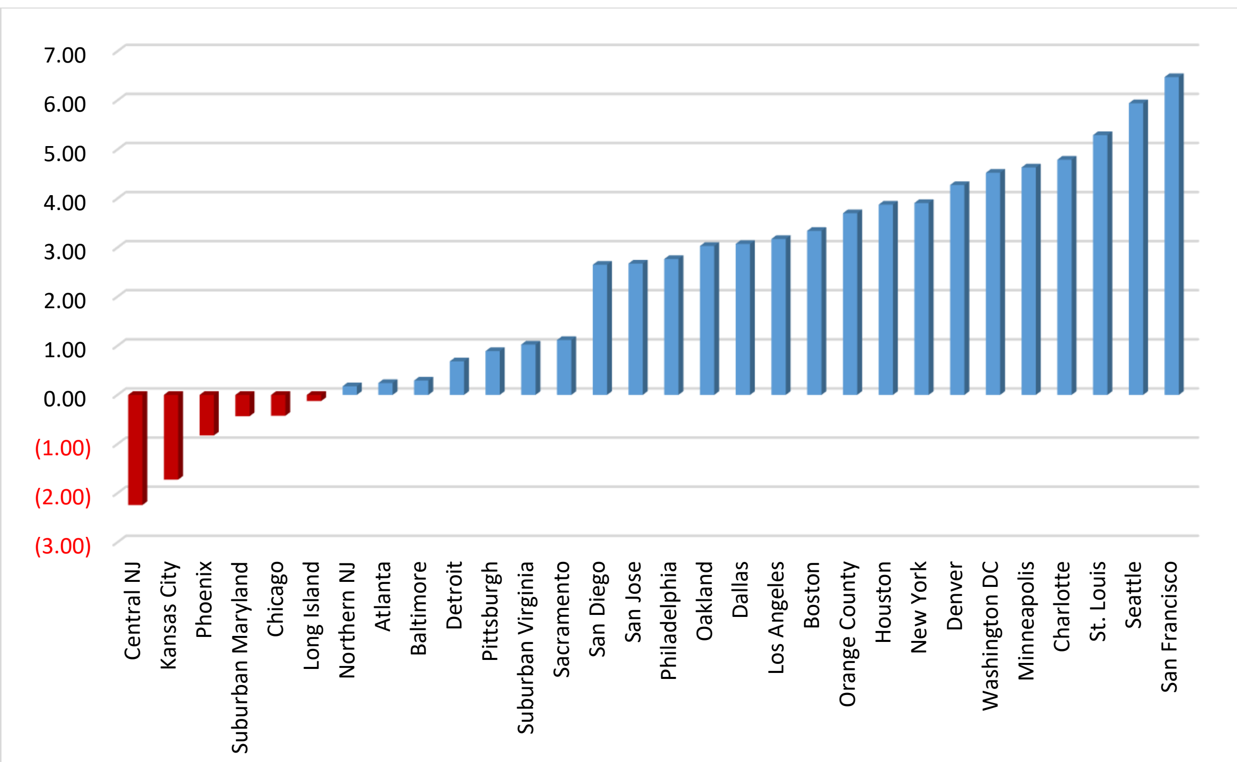
September 2023

Empty Offices and Rising CMBS Loan Delinquency

Vacancy Remains Elevated for Office Space but Historically Low for Industrial Space

Latest data shows that vacancy rate for office space remains substantially elevated compared to the pre-pandemic level across 30 major U.S. markets. Figure 1 shows the change in vacancy rate as of Q2 2023, compared to the pre-pandemic average (Q1 2017 to Q4 2019). San Francisco and Seattle—two major technology hubs—top the list of cities with the largest increase in office vacancy. On the other spectrum, Central New Jersey, Kansas City, and Phoenix headline places that have attracted more office tenants now than before the pandemic.

Figure 1: *Change in Office Space Vacancy Rate, Q2 2023 Compared to Pre-Pandemic Average*[1]



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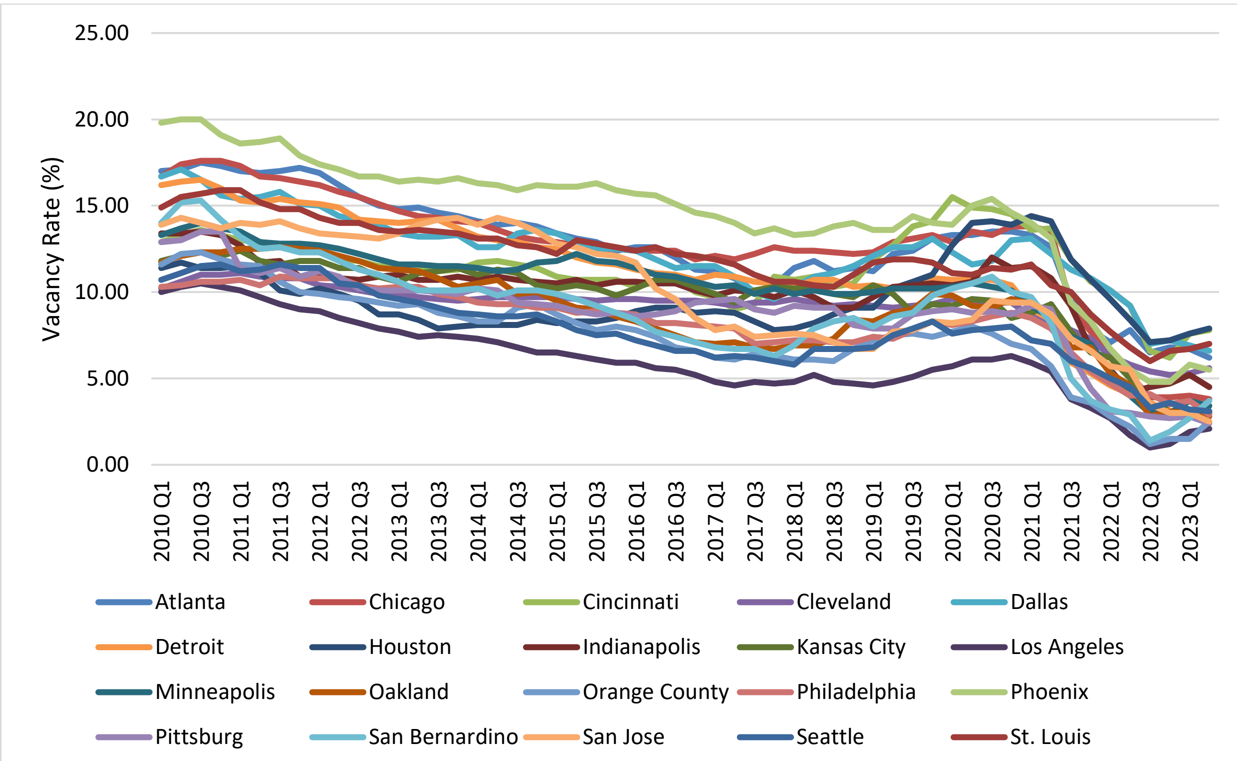
[1] "Office Space Vacancy Rate." *Bloomberg Intelligence*.

Industrial space is a different story entirely. Across major markets, the vacancy rate for industrial space has declined drastically during the pandemic, possibly driven by the massive shifts in consumers spending towards e-commerce and the resulting increased demand for warehousing. Despite a visible uptick in vacancy rate towards the end of 2022, the market for industrial space remains extremely tight overall. As Figure 2 shows, the current vacancy rate is well below 10 percent across the top 20 markets. It remains to be seen whether the historically low vacancy rate reflects a structural shift for this market segment or some regression to the mean would transpire in the months to come.

Figure 2: *Vacancy Rate for Industrial Space, Q1 2010 to Q2 2023*[2]



<u>**Delinquency on the Rise for CMBS Loans for Office Space**</u>

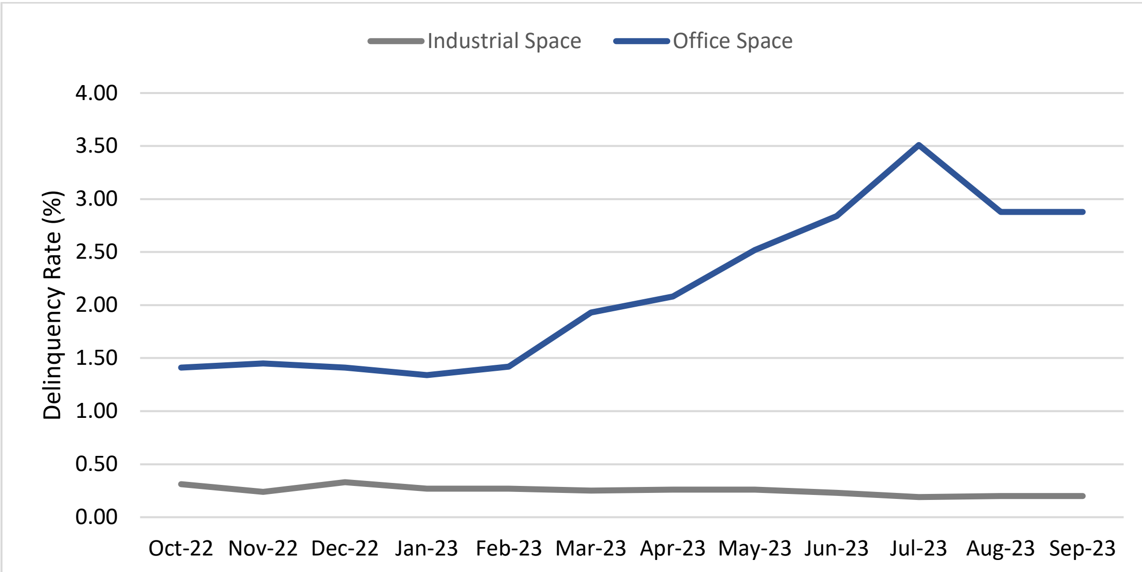
Over the past decade, investors have shown a strong appetite for commercial mortgage-backed securities ("CMBS"). That continued during the pandemic. In 2021, annual CMBS issuance surpassed $250 billion for the first time since the 08/09 financial crisis. The elevation in vacancy rate for office space has sparked concerns over the performance of the CMBS loans for office buildings. Some saw the recent spike in 60-plus-day delinquency rate—from 1.5 percent to 3.5 percent over Q2 2023—as a first sign of trouble to come for these loans (*see* Figure 3). Others view the overall low rate of delinquency as evidence of strength in the market instead.

Delinquency rates for CMBS loans for industrial properties, on the other hand, have been effectively zero for the past 12 months. This is hardly surprising considering the strong market

[2] "Industrial Space Vacancy Rate." *Bloomberg Intelligence*.

demand for industrial space conveyed by the segment's exceptional low vacancy rate across the U.S.

Figure 3: *60-Plus-Day Delinquency Rate for CMBS Loans, October 2022 to September 2023*[3]



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[3] "CMBS Market Overview." *Bloomberg Intelligence*.